



CITY OF SAN JOSÉ, CALIFORNIA

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GERALD A. SILVA
City Auditor

August 22, 1986

Honorable Mayor and Members
of the City Council
801 North First Street, Room 600
San Jose, CA 95110

Transmitted herewith is a report on the May/June 1986
Compliance Review of City Investment Transactions. This report
is in accordance with City Charter Section 805(a).

An Executive Summary is presented on the blue papers in the
front of this report while the Administration response (Finance
Department) is shown on the yellow pages after the Attachments.

I will present this report to the Finance Committee at its
September 15, 1986 meeting. If you need additional information
in the interim, please let me know. City Auditor staff who
participated in the preparation of this report are Nancy
Keeley, Dominador Melendez and Nestor Baula.

Respectfully submitted,

Gerald A. Silva
City Auditor

GS:g
0098

cc: Gerald Newfarmer, City Manager
Les White, Assistant City Manager
Edward G. Schilling, Director of Finance
Susan George, Deputy City Manager
Deborah Kelly, City Treasurer
Emily Harrison, Chief of Accounting
Jessica Batinich, Treasury Assistant



OFFICE OF THE
CITY AUDITOR

**A COMPLIANCE AUDIT OF THE CITY
AND REDEVELOPMENT AGENCY INVESTMENT
PROGRAMS FOR
MAY AND JUNE 1986**

A REPORT TO THE
SAN JOSE
CITY COUNCIL

AUGUST 1986

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EXECUTIVE SUMMARY

In response to an August 5, 1985 Council Finance Committee request, the City Auditor has initiated a process for monthly reviews of investments for the City and the Redevelopment Agency. These reviews have resulted in recommendations to improve the investment program. Finance is taking steps to implement the City Auditor's recommendations to correct the problems noted during the monthly reviews.

Our review of investment transactions for the City and the Redevelopment Agency for May and June 1986 indicates that Finance has generally complied with Investment Policy requirements. We did note 1) untimely City confirmation of investment purchase transactions and 2) Redevelopment Accounting is not date-stamping dealer confirmations, safekeeping receipts/releases, and debit and credit advices.

Noncompliance continues in those areas which require more in-depth staff work and legal assistance. These areas include evaluating dealer financial condition, executing formal dealer and safekeeping agreements and expediting delivery of transaction confirmations. Improvements in documentation and control procedures are occurring. Audit staff will continue to

monitor such improvements until Finance staff becomes familiar with new procedures. Appendix A contains an overview of this review.

The City Auditor has developed a number of recommendations to enhance compliance with the City's Investment Policy and improve the City's investment program. Our review indicates that Finance is taking steps to comply with prior audit recommendations. Of the twenty-eight recommendations contained in the Reviews of September, October, November/December 1985, January/February 1986 and March/April 1986 investments:

- o Fourteen have been fully implemented,
- o Two are combined with other recommendations,
- o Four are implemented, but procedures need improvement, and
- o Eight are in progress

Refer to Appendix B for an overview of Implementation Status.

It is recommended that:

Recommendation #1:

Treasury log the dates confirmations, which outline instructions and details for transactions entered into over the telephone, were mailed to banks.

Recommendation #2:

Redevelopment Accounting date-stamp dealer confirmations, safekeeping receipts/releases and debit and credit advices as received. (Priority 2)

THE MAY AND JUNE 1986 REVIEW:
-GENERAL COMPLIANCE OCCURRING
-UNTIMELY CONFIRMATION OF INVESTMENT
TRANSACTIONS
-REDEVELOPMENT ACCOUNTING NOT
DATE STAMPING DOCUMENTS

Our review of investment transactions for the City and the Redevelopment Agency for May and June 1986 indicates that Finance has generally complied with Investment Policy requirements. We did note 1) untimely City confirmation of investment purchase transactions and 2) Redevelopment Accounting is not date-stamping dealer confirmations, safekeeping receipts/releases and debit and credit advices.

Noncompliance continues in areas which require more in-depth staff work and legal assistance. These areas include evaluating dealer financial condition, executing formal dealer and safekeeping agreements and expediting delivery of transaction confirmations. Improvements in documentation and control procedures are occurring. Audit staff will continue to monitor such improvements until Finance staff become familiar with the procedures. Appendix A contains an overview of the results of this review.

Dealer Prequalification

The City Treasury has generally complied with policy requirements on dealer prequalification. Treasury and the City

Attorney's Office are still in the process of drafting the dealer service agreement, which includes master repurchase provisions.

Purchases

Our review of investment transactions indicates that Finance complied with Investment Policy purchasing requirements during May and June 1986 except for untimely City confirmation of investment purchase transactions and lack of date-stamping of Redevelopment Accounting documents.

Untimely City Confirmations

The City's Investment Policy states in part:

"A written confirmation outlining details for the transactions and confirming the telephoned instructions will be sent to the bank within five working days".

Of the 151 investment purchase transactions entered into by the City and Redevelopment Agency during May and June 1986, 25 were not confirmed in writing within five working days. Another 56 confirmations were not dated and we were unable to

determine the number of days between transactions and confirmation for these purchases.

In the latter part of June 1986, Treasury started logging the mailing dates of confirmations. This procedure will help ensure that future City confirmations will be issued on time.

Lack of Date-Stamping

Redevelopment Agency Accounting does not date stamp dealer confirmations, safekeeping receipts/releases, and debit and credit advices the Agency receives. Without the date stamping it is not possible to document the timeliness of dealer and safekeeping agent confirmations and the related reconciliation of purchase documents.

In the City Auditor's Compliance Audit of the City and Redevelopment Agency Investment Programs for October 1985, the following observations was made:

"...Our review indicated that the Accounting Division is not reconciling the safekeeping "receipts". Instead "receipts" are placed in the investment folder, but are not matched to the confirmation. Accounting staff do not date stamp safekeeping receipts, so it is not possible to verify when they are received..."

Accordingly, the following recommendation was made:

"...Finance establish additional procedures to insure that controls are functioning and written verification of purchases and sales is complete and timely. Specifically, procedures need to be established to ...4) date stamp and reconcile dealer, safekeeping, debit and credit advices as received. (Priority 2)..."

Since the issuance of the October Report, Finance has complied with the above recommendation. In our opinion, Redevelopment Agency Accounting should implement similar procedures to document compliance with the City's Investment Policy.

Except as noted above, Finance complied with Investment Policy purchasing requirements during May and June 1986. Repurchase agreements met Policy collateral requirements. Procedures to document market condition and purchase strategy were followed.

Portfolio Mix

Our review indicated that Finance complied with Policy requirements for portfolio diversification.

Safekeeping

The target date for the completion of formal safekeeping agreements, currently in draft form, has been moved to August 18, 1986. The City Attorney's Office is still reviewing the contract form.

In earlier reviews, we reported that safekeeping receipts were not being reconciled with Treasury confirmation documents. The Accounting Division is now reconciling safekeeping receipts to Accounting's copy of Treasury's confirmation document. Also, Accounting is following up on safekeeping release forms not received on time.

Other Procedures/Controls

Treasury has implemented some improvements in the documentation of cash flow information. However, the accuracy of the cash flow forecast and the usefulness of the documentation for the purpose of a third party review is still limited. Detailed procedures on MONEymax operations have been completed and will be updated as required.

CONCLUSION

Our review of May and June 1986 investment transactions indicated general compliance with the City Investment Policy. The deficiencies we noted are 1) untimely City confirmation of investment purchases transactions and 2) Redevelopment Accounting is not date-stamping dealer confirmations, safekeeping receipt/releases, and debit and credit advices. Finance continues to make progress on implementing prior audit recommendations.

RECOMMENDATION

It is recommended that:

Recommendation #1:

Treasury log the dates confirmations, which outline instructions and details for transactions entered into over the telephone, were mailed to banks.

Recommendation #2:

Redevelopment Accounting date-stamp dealer confirmations, safekeeping receipts/releases, and debit and credit advices as received. (Priority 2)

FOLLOW-UP ON PRIOR RECOMMENDATIONS

The City Auditor has developed a number of recommendations to enhance compliance with the City's Investment Policy and improve the City's investment program. Our review indicates that Finance is taking steps to comply with prior audit recommendations. Of the twenty-eight recommendations contained in the Reviews of September, October, November/December 1985, January/February 1986 and March/April 1986 Investments:

- o Fourteen have been fully implemented,
- o Two are combined with other recommendations,
- o Four are implemented, but procedures need improvement, and
- o Eight are in progress.

Following is an implementation status report for prior recommendations. An overview chart showing the implementation status of prior recommendations is contained in Appendix B.

September 1985 Investment Review

Recommendation #1:

Treasury staff utilize MONEymax in managing the portfolio and making investment decisions by: running a portfolio profile daily or on each day when purchases, sales or maturities occur; and using the portfolio report in making investment decisions.
(Priority 1)

Status:

Implemented.

Recommendation #2:

Treasury staff insure that entry MONEymax is timely and accurate by: entering the transaction data on the date that the transaction occurs; running machine numbered, logged and dated batch reports for all entries; and reviewing batch reports for accuracy. (Priority 1)

Status:

Implemented.

Recommendation #3:

Finance enhance staff's ability to utilize MONEYMAX by: providing comprehensive training for employees in the use of MONEYMAX; and preparing a simplified instructions manual on the use of MONEYMAX for Finance employees. (Priority 2)

Status:

Implemented.

Recommendation #4:

Treasury staff advise Finance management of portfolio status on a timely basis by distributing a copy of the portfolio profile report in Recommendation #1 to the Treasurer, Chief of Accounting and the Finance Director. (Priority 1)

Status:

Implemented.

Recommendation #5:

Treasury staff prepare revenue vouchers for maturities, sales and interest payments on the date funds are deposited or payment is received. (Priority 1).

Status:

Implemented.

Recommendation #6:

Treasury staff maintain documentation to verify information used each day in making investment decisions, including the portfolio profile report and all cash flow information. (Priority 2)

Status:

Implemented.

Recommendation #7:

Finance complete procedures regarding prequalification of financial institutions. (Priority 1)

Status:

This recommendation is now included in Recommendation 3 of the October Investment Review.

Recommendation #8:

Treasury document reasons for sales.

Status:

Based on earlier reviews, documentation for the sale of investments has improved. No sale was made during the period under review. As a result, documentation could not be evaluated.

Further follow-up required.

Recommendation #9:

Accounting complete improvements in reconciliation procedures.

Status:

The intent of this recommendation is now included in Recommendations 7 and 12 in the review of October transactions.

October 1985 Investment Review

Recommendation #1:

Finance comply with Policy requirements to execute formal safekeeping agreements with the City and Redevelopment Agency's Custodial Agents to assure that the City's interest in securities is adequately perfected. (Priority 1)

Status:

A draft safekeeping agreement is still undergoing legal review. Because of a change in City's bank, the target date for the execution of the safekeeping agreement has been moved to August 18, 1986.

Further follow-up is required.

Recommendation #2:

Treasury staff insure that entry MONEYMAX is timely and accurate by: entering the transaction date on the date that the transaction occurs; running machine numbered, logged and dated batch reports for all entries; and reviewing batch reports for accuracy. (Priority 1)

Status:

Implemented.

Recommendation #3:

Finance comply with Policy requirements to establish procedures to evaluate and monitor dealer financial condition and execute formal master repurchase agreements and services agreements with dealers. (Priority 1)

Status:

Treasury has completed draft procedures for evaluating financial statements. The evaluation process has begun and will continue as time allows. The City Attorney's Office is reviewing a draft dealer service agreement which includes master repurchase provisions. Finance has been working directly with the City Attorney's Office to finalize the dealer service agreement. No target date for execution of agreement was provided.

Further follow-up is required.

Recommendation #4:

Treasury establish guidelines for repurchase agreements which 1) allow substitution of securities only on an exception basis, and 2) limit the number of securities used as collateral. Treasury document reasons for exceptions to the guidelines. (Priority 1)

Status:

Implemented.

Recommendation #5:

Finance obtain clarification from the Private Sector Investment Committee regarding the issues of repurchase agreement collateral, issuer percentages, and financial institution qualifications. (Priority 2)

Status:

Implemented.

Recommendation #6:

Finance include in its Monthly Investment Report all investments which do not comply with Policy provisions. Finance should indicate which investments are subject to on-going review for potential sale. (Priority 2)

Status:

Implemented.

Recommendation #7:

Accounting ensure that safekeeping receipts are promptly received and reconciled. (Priority 1)

Status:

Implemented.

Recommendation #8:

Treasury establish data entry standards to ensure the accuracy of MONEymax entry, including adequate issuer identification. (Priority 1)

Status:

Implemented.

Recommendation #9:

Treasury enter the dealer's name and securities held as collateral for repurchase agreements into the MONEYMAX system.
(Priority 1)

Status:

Implemented.

Recommendation #10:

Treasury document daily investment strategy and purchase decisions. (Priority 2)

Status:

Treasury is becoming more familiar with the new procedures. Significant improvements have been made.

Further follow-up is required.

Recommendation #11:

Treasury segregate the functions of investing funds and receiving investment income. (Priority 1)

Status:

Treasury has implemented an alternative procedure. The Chief of Treasury or a designee not directly involved in placing investments now approve investment-related revenue vouchers.

Further follow-up is required.

Recommendation #12:

Finance establish additional procedures to ensure that controls are functioning and written verification of purchases and sales is complete and timely. Specifically, procedures need to be established to 1) monitor compliance with Policy provisions regarding release of funds or securities 2) provide for 24 hour preparation and mailing of confirmations 3) implement pre-numbered and controlled confirmation documents and 4) date stamp and reconcile dealer, safekeeping, debit and credit advices as received. (Priority 2)

Status:

The Control Log for wire transfer of funds has been properly initialed since November 1985. The revised Investment Policy now allows for five working days for transmittal of confirmations. Implementation of pre-numbered confirmation documents is targeted for August 15, 1986 in order that automation of forms through MONEYMAX can be explored. City Accounting is now date stamping all receipts and advices. Redevelopment Accounting has agreed to purchase a date stamp and to start date stamping all dealer, safekeeping, debit and credit advices as received.

Partially implemented.

November-December 1985 Investment Review

Recommendation #1:

Finance obtain a legal opinion to determine requirements for an independent third party custodian for securities involved in City investments. (Priority 2)

Status:

Finance has ceased executing repurchase agreements with the banks which serve as the safekeeping agents for the City

and the Redevelopment Agency portfolios. The issue of third party custodians may be addressed in the legal review of the proposed safekeeping agreements. Execution of safekeeping agreements is anticipated by August 18, 1986.

Further follow-up is required.

Recommendation #2:

Finance incorporate a clause in the proposed City-initiated dealer agreements to supersede any prior service or master repurchase agreements with the dealer. (Priority 2)

Status:

Finance will include the recommended clause in the master repurchase agreement now under review by legal counsel. No target date has been set to mail the agreements to dealers.

Further follow-up is required.

Recommendation #3:

Finance document its Policy interpretations. (Priority 2)

Status:

Finance will have the Policy interpretations documented in final form by September 1, 1986.

Further follow-up is required.

March-April 1986 Investment Review

Recommendation #1:

Finance obtain Private Sector Panel approval of alternative dealer financial information requirements and amend the Investment Policy accordingly. (Priority 2)

Status:

Finance has explored several alternatives to deal with the problems of evaluating firms such as a private partnership which would not provide its profit and loss statement. Finance will propose to the Private Sector Panel that a SEC-registered private partnership be screened on two factors as follows:

- o disclosure of its excess net capital in the notes to the statement of financial condition, and

- o a separate letter from its CPA firm attesting to the facts that Rule 15c 3-1 has been complied with and the dealer's internal systems and controls have no material inadequacies. Rule 15c 3-1 states that a dealer's liquid capital, reduced by its measured risk, must exceed the dealer's obligations to its customers on a continuous basis.

The Private Sector Panel will meet sometime in September or October, 1986 to consider these alternative dealer financial information requirements.

Further follow-up is needed.

Recommendation #2:

Finance include in the Investment Procedures specific instructions regarding all Policy provisions. These instructions should address 1) all required dealer financial information requirements 2) dealer acknowledgement of the City's Investment Policy 3) pre-formatted wire instructions for banks and 4) instrument and issuer ratings. (Priority 2)

Status:

The Treasurer has issued to the staff instructions on issuer and dealer prequalification including 1) all required dealer financial information requirements, 2) dealer acknow-

ledgement of the City's Investment Policy, 3) pre-formatted wire instructions for banks, and 4) instrument and issuer ratings. Further follow-up is required to ascertain that the instructions are followed and included in the Investment Procedures.

Recommendation #3:

Finance report all technical exceptions to the City's Investment Policy to the Finance Committee in its Monthly Investment Report. (Priority 2)

Status:

Finance will include in its Monthly Investment Report technical exceptions in Exhibit D of the Executive Summary.

Further follow-up is required.

CITY OF SAN JOSE - MEMORANDUM

TO: Honorable Mayor and City Council FROM: Edward G. Schilling
Director of Finance

SUBJECT: RESPONSE TO AUDITOR'S MAY/JUNE 1986 COMPLIANCE REVIEW DATE: August 20, 1986

APPROVED



DATE

BACKGROUND

The Finance Department and the City Auditor's office continue to devote significant levels of effort to fulfilling their important responsibilities with regard to the City's Investment Program. Staff members in both of these offices have reason to be proud of their respective contributions to the development of a very well-managed program which must be able to withstand the closest of scrutiny. The May/June Compliance Review has resulted in two additional recommendations for procedural improvements, both of which were implemented before the issuance of the City Auditor's draft report. Those recommendations and their associated responses follow.

RECOMMENDATION #1

Treasury log the dates confirmations, which outline instructions and details for transactions entered into over the telephone, were mailed to banks.

RESPONSE

As stated in the body of the May/June 1986 Compliance Review, Treasury established the log described in this recommendation in the latter part of June 1986. It required a few weeks for the maintenance of the log to become a fixed part of the daily routine. Treasury has maintained the log on a daily basis since mid-July and will continue to do so.


RECOMMENDATION #2

Redevelopment Accounting date-stamp dealer confirmations, safekeeping receipts/released and debit and credit advices as received. (Priority 2)

RESPONSE

Redevelopment Accounting had already installed a date-stamp machine before the draft audit report was disseminated. They are date-stamping all incoming investment documents.

Respectfully submitted,


Edward G. Schilling
Director of Finance

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CITY AUDITOR

APPENDIX A

SUMMARY OF COMPLIANCE QUESTIONS FOR REVIEW OF MAY 1986 AND JUNE 1986 INVESTMENT TRANSACTIONS OF THE CITY AND THE REDEVELOPMENT AGENCY

<u>Compliance Question</u>		Based on Sample Review of Finance Documentation Did all Transactions Meet Criteria?	
		<u>May 1986</u>	<u>June 1986</u>
A. PREQUALIFICATION OF DEALERS			
1.	Is the Dealer (1) on the list of Government Security Dealers Reporting to the Market Reports Division of Federal Reserve, or does the dealer meet the required Keefe, Bruyette and Woods rating?	YES	YES
2.	Has the Dealer or Bank filed an acknowledgement of receipt and review of the City's Investment Policy with Treasury?	YES	YES
3.	Have Financial Statements been filed with Treasury?	YES	YES
4.	Do the Financial Statements include a Balance Sheet and a Profit and Loss Statement?	NO	NO
5.	Are the Financial Statements current?	YES	YES
6.	Has Treasury reviewed the Financial Statements?	NO	NO
7.	Has a Services Agreement been executed?	NO	NO

(1) Includes banks and savings and loans acting as dealers. Treasury accepts a Keefe, Bruyette and Woods rating of "B", or "C" for selected major California banks, in lieu of primary dealer status for banks and savings and loans.

APPENDIX A

SUMMARY OF COMPLIANCE QUESTIONS FOR REVIEW OF MAY 1986 AND JUNE 1986 INVESTMENT TRANSACTIONS OF THE CITY AND THE REDEVELOPMENT AGENCY

Based on Sample Review
of Finance Documentation
Did all Transactions
Meet Criteria?

<u>Compliance Question</u>	<u>May 1986</u>		<u>June 1986</u>	
B. PROVISIONS APPLYING TO ALL PURCHASES				
1. Purchase is of an approved instrument?	YES		YES	
2. Purchase Maturity is within policy limits for instrument?	YES		YES	
3. Wire Transfer of funds initiated by employee other than employee initiating investment?	YES		YES	
4. Wire Transfer of funds carried out according to the terms of preformatted Wire Transfer letter?	YES		YES	
C. PORTFOLIO MIX				
1. Is within Policy limits for category of instruments?	YES		YES	
2. Total with a single issuer, other than government issues:				
a) Is within 10% of total portfolio, unless an overnight repo?	YES		YES	
b) For uninsured-uncollateralized issues, is within 5% of total portfolio?	YES		YES	
D. TIME DEPOSITS - BANKS AND SAVINGS AND LOANS				
1. Bank or savings and loan is located in San Jose area (Santa Clara County)?	NONE		NONE	

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SUMMARY OF COMPLIANCE QUESTIONS FOR REVIEW OF MAY 1986 AND JUNE 1986 INVESTMENT TRANSACTIONS OF THE CITY AND THE REDEVELOPMENT AGENCY

<u>Compliance Question</u>		Based on Sample Review of Finance Documentation Did all Transactions Meet Criteria?	
		<u>May 1986</u>	<u>June 1986</u>
2.	If not San Jose area, is it a minority bank?	NONE	NONE
3.	Is a Contract for Public Funds Deposit on file?	NONE	NONE
4.	Is a Waiver for Collateralization on file (for insured portion)?	NONE	NONE
5.	For uninsured portion (over \$100,000), is the deposit with a bank or savings and loan with a Keefe, Bruyette and Woods rating of "B" or better, unless a "selected California bank" (Bank of America or Wells Fargo) rated "C" or better?	NONE	NONE
E. U. S. GOVERNMENT AGENCY ISSUES			
1.	Is issue by one of the following: o Federal Farm Credit Bank; o Federal Home Loan Bank (including FHLMC) or o Federal National Mortgage Association?	YES	YES
F. REPURCHASE AGREEMENTS			
1.	Collateral is U.S. Treasury or Government Agency issue approved for purchase by Policy?	YES	YES
2.	If overnight, collateral is equal to 100% of the repurchase agreement's face value?	YES	YES

APPENDIX A

SUMMARY OF COMPLIANCE QUESTIONS FOR REVIEW OF MAY 1986 AND JUNE 1986 INVESTMENT TRANSACTIONS OF THE CITY AND THE REDEVELOPMENT AGENCY

		Based on Sample Review of Finance Documentation Did all Transactions Meet Criteria?	
<u>Compliance Question</u>		<u>May 1986</u>	<u>June 1986</u>
3.	If other than overnight, collateral is marked-to-market on a daily basis and maintained equal to 100% of the repurchase agreement's face value; or is sufficiently in excess of the repurchase agreements face value?	NONE	NONE
G.	REVERSE REPURCHASE	NONE	NONE
H.	BANKER'S ACCEPTANCES		
1.	Is the issuer a bank or savings and loan with a Keefe, Bruyette and Woods rating of "B" or better, unless a "selected major California bank" (Bank of America or Wells Fargo) rated "C" or better?	YES	YES
I.	NEGOTIABLE CERTIFICATES OF DEPOSIT		
1.	Is the issuer a bank or savings and loan with a Keefe, Bruyette and Woods rating of "A/B" or better?	NONE	NONE
J.	COMMERCIAL PAPER		
1.	Is this a domestic corporation?	YES	YES
2.	Does this institution have the highest rating by Moody's or Standard and Poor's?	YES	YES
3.	Does this institution have total assets of \$500,000,000 or more?	YES	YES
4.	Does this institution have an "A" rating or higher on its own indebtedness other than its commercial paper?	YES	YES

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SUMMARY OF COMPLIANCE QUESTIONS FOR REVIEW OF MAY 1986 AND JUNE 1986 INVESTMENT TRANSACTIONS OF THE CITY AND THE REDEVELOPMENT AGENCY

<u>Compliance Question</u>	Based on Sample Review of Finance Documentation Did all Transactions Meet Criteria?	
	<u>May 1986</u>	<u>June 1986</u>
K. SAFEKEEPING-TREASURY PROCEDURES		
1. Person initiating release of securities is not same person initiating sale?	NONE	NONE
2. Written confirmation for release of City-owned securities was transmitted to Safekeeper within 5 working days of telephone instructions.	NONE	NONE
L. SAFEKEEPING - SECURITY/COLLATERAL HELD		
1. Collateral held by a Safekeeping Agent under the terms of a Safekeeping Agreement with the City?	NO	NO
2. For securities serving as collateral for a repurchase agreement which are not held by a Safekeeping Agent, are the securities held by a third party custodian with a Safekeeping Agreement with the City?	NONE	NONE
3. For uninsured/collateralized Time Deposits in a savings and loan, is collateral held by the Federal Home Loan Bank?	NONE	NONE

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SUMMARY OF COMPLIANCE QUESTIONS FOR REVIEW OF MAY 1986 AND JUNE 1986 INVESTMENT TRANSACTIONS OF THE CITY AND THE REDEVELOPMENT AGENCY

		Based on Sample Review of Finance Documentation Did all Transactions Meet Criteria?	
<u>Compliance Question</u>		<u>May 1986</u>	<u>June 1986</u>
4.	For uninsured/collateralized Time Deposits in a bank, is collateral held in the City's name in:		
	a) The issuing banks' trust department, provided the bank has a Safekeeping Agreement with the City, or	NONE	NONE
	b) In the San Francisco Federal Reserve Bank?	NONE	NONE
M. REPORTING			
1.	Exceptions reported to Finance Committee?	YES	YES
<u>OTHER AREAS</u>			
1.	Was sale necessary to meet cash needs?	NONE	NONE

APPENDIX B

SUMMARY OF IMPLEMENTATION STATUS FOR PRIOR RECOMMENDATIONS

<u>Recommendation</u>	<u>Status</u>
<u>REVIEW OF SEPTEMBER 1985 INVESTMENTS</u>	
<u>Recommendation #1</u> Treasury staff utilize MONEymax in managing the portfolio and making investment decisions by: running a portfolio profile daily or on each day when purchases, sales or maturities occur; and using the portfolio profile report in making investment decisions. (Priority 1)	Implemented
<u>Recommendation #2</u> Treasury staff insure that entry into MONEymax is timely and accurate by: entering transaction data on the date that the transaction occurs; running machine numbered, logged and dated batch reports for all entries; and reviewing batch reports for accuracy. (Priority 1)	Implemented
<u>Recommendation #3</u> Finance enhance staff's ability to utilize MONEymax by: providing comprehensive training for employees in the use of MONEymax; and preparing a simplified instruction manual on the use of MONEymax for Finance employees. (Priority 2)	On June 3, 1986 the Treasury staff attended training sessions for Gateway and cash flow requirements, and general review of MONEymax system as needed. Training will be on going. Implemented.

APPENDIX B

SUMMARY OF IMPLEMENTATION STATUS
FOR PRIOR RECOMMENDATIONS

<u>Recommendation</u>	<u>Status</u>
<u>Recommendation #4</u> Treasury staff advise Finance management of portfolio status on a timely basis by distributing a copy of the portfolio profile report in Recommendation #1 to the Treasurer, Chief of Accounting and the Finance Director. (Priority 1)	Implemented
<u>Recommendation #5</u> Treasury staff prepare revenue vouchers for maturities, sales and interest payments on the date funds are deposited or payment is received. (Priority 1)	Implemented.
<u>Recommendation #6</u> Treasury staff maintain documentation to verify information used each day in making investment decisions, including the portfolio profile report and all cash flow information. (Priority 2)	Implemented.
<u>Recommendation #7</u> Finance complete procedures regarding prequalification of financial institutions.	Included in Recommendation #3 of the October Investment Review.
<u>Recommendation #8</u> Treasury document reasons for sales.	Further follow-up required.

APPENDIX B

SUMMARY OF IMPLEMENTATION STATUS FOR PRIOR RECOMMENDATIONS

<u>Recommendation</u>	<u>Status</u>
<u>Recommendation #9</u> Accounting complete improvements in reconciliation procedures.	 This recommendation is now included in Recommendation #7 and 12 of the the October Investment Review.
<u>REVIEW OF OCTOBER 1985 INVESTMENTS</u>	
<u>Recommendation #1</u> Finance comply with Policy requirements to execute formal safekeeping agreements with the City and Redevelopment Agency's Custodial Agents to assure that the City's interest in securities is adequately perfected. (Priority 1)	 Draft agreement still undergoing legal review. City's Bank will be changed effective August 18, 1986. Execution of City safekeeping agreements is anticipated by August 18, 1986. Redevelopment Agency safekeeping agreement is still being reviewed by agency legal counsel. No target date for execution was stated. Further follow-up is required.
<u>Recommendation #2</u> Treasury staff comply with Policy requirements to maintain collateral at 100% of the repurchase agreement's face value, marked-to-market value daily, or sufficiently in excess of the agreement's face value. (Priority 1)	 Implemented.

APPENDIX B

SUMMARY OF IMPLEMENTATION STATUS FOR PRIOR RECOMMENDATIONS

<u>Recommendation</u>	<u>Status</u>
<u>Recommendation #3</u> Finance comply with Policy requirements to establish procedures to evaluate and monitor dealer financial condition and execute formal master repurchase agreements and services agreements with dealers. (Priority 1)	Evaluation procedures are in draft form. Evaluations started and will continue as time allows. City Attorney's Office is reviewing a draft dealer service agreement which includes master repurchase provisions. Finance Director has been working directly with the City Attorney's Office to finalize the dealer service agreements. No target date for execution of agreement could be provided. Further follow-up required.
<u>Recommendation #4</u> Treasury establish guidelines for repurchase agreements which 1) allow substitution of securities only on an exception basis, and 2) limit the number of securities used as collateral. Treasury document reasons for exceptions to the guidelines. (Priority 1)	Implemented.
<u>Recommendation #5</u> Finance obtain clarification from the Private Sector Investment Committee regarding the issues of repurchase agreement collateral, issuer percentages, and financial institution qualifications. (Priority 2)	Implemented.

APPENDIX B

SUMMARY OF IMPLEMENTATION STATUS FOR PRIOR RECOMMENDATIONS

<u>Recommendation</u>	<u>Status</u>
<u>Recommendation #6</u> Finance include in its Monthly Investment Report all investments which do not comply with Policy provisions. Finance should indicate which investments are subject to on-going review for potential sale. (Priority 2)	Implemented.
<u>Recommendation #7</u> Accounting ensure that safe-keeping receipts are promptly received and reconciled. (Priority 1)	Implemented.
<u>Recommendation #8</u> Treasury establish data entry standards to ensure the accuracy of MONEymax entry, including adequate issuer identification. (Priority 1)	Implemented.
<u>Recommendation #9</u> Treasury enter the dealer's name and securities held as collateral for repurchase agreements into the MONEymax system. (Priority 1)	Implemented.

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SUMMARY OF IMPLEMENTATION STATUS FOR PRIOR RECOMMENDATIONS

<u>Recommendation</u>	<u>Status</u>
<u>Recommendation #10</u> Treasury document daily investment strategy and purchase decisions. (Priority 2)	Implemented. Requires further monitoring.
<u>Recommendation #11</u> Treasury segregate the functions of investing funds and receiving investment income. (Priority 1)	Alternative procedures implemented. The Chief of the Treasury or designee not involved in investment activities approves revenue vouchers. Further follow-up required.
<u>Recommendation #12</u> Finance establish additional procedures to ensure that controls are functioning and written verification of purchases and sales is complete and timely. Specifically, procedures need to be established to 1) monitor compliance with Policy provisions regarding release of funds or securities 2) provide for 24 hour preparation and mailing of confirmations 3) implement pre-numbered and controlled confirmation documents and 4) date stamp and reconcile dealer, safekeeping, debit and credit advices as received. (Priority 2)	Partially implemented. The Control Log for wire transfer of funds has been properly initialed. The revised Investment Policy now allows five working days for transmittal of confirmations. Treasury has started logging dates confirmations are mailed to monitor and document compliance. Implementation of pre-numbered confirmations is targeted for August 15, 1986. City Accounting is now date stamping all receipts and advices. Redevelopment Accounting is not date stamping receipts and advices.

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SUMMARY OF IMPLEMENTATION STATUS FOR PRIOR RECOMMENDATIONS

REVIEW OF NOVEMBER-DECEMBER 1985 INVESTMENTS

<u>Recommendation</u>	<u>Status</u>
<u>Recommendation #1:</u> Finance obtain a legal opinion to determine requirements for an independent third party custodian for securities involved in City investments. (Priority 2)	Finance has stopped executing repurchase agreements with the bank which safekeeps that portfolio's securities. The issue of a third party custodian will be addressed in the proposed safekeeping agreement.
<u>Recommendation #2:</u> Finance incorporate a clause in the proposed City-initiated dealer agreements to supersede any prior service or master repurchase agreements with the dealer. (Priority 2)	Finance will include the recommended clause in the master repurchase agreement now under review by legal counsel.
<u>Recommendation #3:</u> Finance document its Policy interpretations. (Priority 2)	Draft was completed and is being reviewed by the Treasury Chief and targeted for completion by September 1, 1986.
<u>Recommendation #4:</u> Finance prepare a compilation and analysis of State and Federal laws applicable to the investment program. (Priority 2)	Implemented.

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SUMMARY OF IMPLEMENTATION STATUS FOR PRIOR RECOMMENDATIONS

REVIEW OF MARCH-APRIL 1986 INVESTMENTS

<u>Recommendation</u>	<u>Status</u>
<u>Recommendation #1:</u> Finance obtain Private Sector Panel approval of alternative dealer financial information requirements and amend the the Investment Policy accordingly. (Priority 2)	Finance will propose to the Private Sector Panel that a SEC-registered private partnership be screened on two factors as follows: 1) disclosure of its excess net capital in the notes to the statement of financial condition, and 2) separate letter from its CPA firm attesting to the facts that Rule 15c 3-1 has been complied with and the dealer's internal systems and controls have no material inadequacies. The Private Sector Panel will meet sometime in September or October, 1986 to consider these alternative dealer financial information requirements.
<u>Recommendation #2:</u> Finance include in the Investment Procedures specific instructions regarding all Policy provisions. These instructions should address 1) all required dealer financial information requirements 2) dealer acknowledgement of the City's Investment Policy 3) pre-formatted wire instructions for banks and 4) instrument and issuer ratings. (Priority 2)	Treasurer has issued to the staff instructions regarding all Policy provisions. These will be incorporated into the Investment Procedures.

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SUMMARY OF IMPLEMENTATION STATUS
FOR PRIOR RECOMMENDATIONS

REVIEW OF MARCH-APRIL 1986 INVESTMENTS

<u>Recommendation</u>	<u>Status</u>
<u>Recommendation #3:</u> Finance report all technical exceptions to the City's Investment Policy to the Finance Committee in its Monthly Investment Report. (Priority 2)	 Beginning in June 1986 Investment Report, Finance has started reporting technical exceptions in Exhibit D of the Executive Summary.